

BEFORE THE STATE BOARD OF EQUALIZATION
OF THE STATE OF CALIFORNIA

Appeals of Ray Manzano and William and Elizabeth Sacchetto

additional balls to be played. The player, however, has no control over the effects which the deposit of additional coins will have.

There are controls inside the machine which can be adjusted in order to change the odds. These adjustments range from liberal to conservative, but the state of adjustment is not evident to the player. The machines are also equipped with anti-tilt controls. If the player jars or tilts the machine **beyond a very limited degree**, this control is activated and voids the player's score. The sensitivity of this control may also be adjusted, but again the state of adjustment is not evident to the player.

A counter in the scoring panel shows the number of free games won by the player. The free plays and the reading on the counter in the scoring panel may be removed by pushing a button set into the case of the machine. Inside the machine is another counter or meter which records the number of free plays which are removed by pushing the button, rather than by playing them. From the record before us, it may be inferred that the purpose of these devices is to facilitate the redemption of free games for cash.

The arrangement between Century and each location owner was that Century was to **maintain** the machine in proper working order, the location owner was to furnish the electricity to operate the machine, Century was to retain the key to the coin box in the machine, and a representative from Century was to visit the location periodically to open the machine, count the coins and wrap them. At the time of the collection, the location owner would inform the representative from Century of the amount of the location owner's expenses in connection with the operation of the machines and this amount would be set aside for him from the amount in the machine. The balance was divided equally between Century and the location owner. The expenses claimed by the location owner might include cash payouts to players in lieu of free games, refunds to players for mechanical malfunction or taxes and licenses assessed against the machine. Generally, the representative of Century did not leave the location with the nickels to which Century was entitled, but the nickels remained with the location owner and he gave the representative of Century paper money and large coins equal to the amount of nickels to which Century was entitled. In this way, the location owner had the nickels which he needed to make change for persons desiring to play the machine.

The amounts which Century obtained out of the machines (that is, total amount going into machines less location owners' expenses and location owners' shares) were reported as gross

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income on the partnership return filed for Century Amusement Company. The auditor for the Franchise Tax Board stated that the assessment was computed on the basis that all the nickels deposited in the machines were the gross income of Century and that no deductions were allowed because in operating the machines, Appellants were engaged in an illegal activity as defined in Section 17359 (now 17297) of the Revenue and Taxation Code. The auditor stated that he determined the total amount deposited in the machines by starting with the reported gross income of Century, adding an equal amount as the location owners' shares and then adding an estimated amount representing payouts in lieu of free games and other expenses initially paid by the location owners but recovered back from the amounts in the machines.

There were no records indicating the amount of payouts and other expenses. Such amount was computed on the assumption that it equaled 50% of the total deposited in each machine. The 50% figure was an estimate given to the auditor by one of the location owners whom the auditor interviewed. The auditor assumed that this 50% figure would be applicable to all the locations which had machines owned by Century.

Two of the location owners testified that they had pinball machines owned by Century and that it was their general practice to make cash payouts to a player in lieu of free games whenever requested by the player. Their testimony as to their arrangements with Century was consistent with what has been stated earlier in this opinion.'

Appellants offered no evidence. The Appellants themselves did not testify.

Section 17359 read:

"In computing net income, no deductions shall be allowed to any taxpayer on any of his gross income derived from illegal activities as defined in Chapters 9, 10 or 10.5 of Title 9 of Part 1 of the Penal Code of California; nor shall any deductions be allowed to any taxpayer on any of his gross income derived from any other activities which tend to promote or to further, or are connected or associated with, such illegal activities."

Section 330a of the Penal Code is in Chapter 10 of Title 9 of Part 1 of the Penal Code and makes it a crime to possess or control a "mechanical device, upon the result of action of which money . . . is . . . hazarded, and which is operated . . . by . . .

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depositing therein any coins ... and by means whereof ... money . . . is won or lost . . . *when* the result of action . . . of such machine ... is dependent on hazard or chance . . ."

From the evidence presented, it can be concluded that money is hazarded on the result of action of the pinball machines and that money is won or lost on such result. The description of these machines is identical to that in the Appeal of C. B. Hall, Sr., Cal. St. Bd. of Equal., December 29, 1958 (CCH 2 Cal. Tax Cases, Par. 201-197), (P-H St. & Loc. Tax Serv., Cal., Par. 58,145). Here, as in that case, the machines were games of chance. Section 17359 of the Revenue and Taxation Code is thus applicable and, accordingly, no deductions may be allowed to Appellants with respect to their gross income from the machines. In the absence of records, the Franchise Tax Board estimated the total amount deposited in the machines. Appellants have offered no evidence that the computation was inaccurate. Under these circumstances, Respondent's computation of that amount is sustained.

Since the relationship between Century and the location owners is the same as that considered by us in the Hall appeal, our conclusion in Hall that the machine owner and each location owner were engaged-a joint venture in the operation of the machines is applicable here. **Respondent's assessments, therefore, must be revised to reduce Century's gross income from 100% of the coins deposited in the machines to 50% of the coins deposited in the machines.**

O R D E R

Pursuant to the views expressed in the Opinion of the Board on file in this proceeding, and good cause appearing therefor,

IT IS HEREBY ORDERED, ADJUDGED AND DECREED, pursuant to Section 18595 of the Revenue and Taxation Code, that the action of the Franchise Tax Board on protests to proposed assessments of

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additional personal income tax against Ray Manzano in the amount of \$1,000.85 for the year 1953, and against William Sacchetto and Elizabeth Sacchetto in the amount of \$636.22 for the year 1953, be and the same is hereby modified in that the gross income is to be recomputed in accordance with the Opinion of the Board. In all other respects, the action of the Franchise Tax Board is sustained.

Done at Sacramento, California, this 8th day of March,
1961, by the State Board of Equalization,

John W. Lynch, Chairman

Richard Nevins, Member

George R. Reilly, Member

Paul R. Leake, Member

_____, Member

ATTEST: Dixwell L. Pierce, Secretary